Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Calderon	Analyst:	Norman Catelli	Bill Number:	AB 122
Related Bills:	See Legislative History	Telephone:	845-5117	Introduced Date:	January 15, 2003
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Manufacturers' Investment Credit/Extend Repeal Date

SUMMARY

This bill would extend the repeal date of the Manufacturers' Investment Credit (MIC), extending the credit until at least January 1, 2006.

This analysis addresses only those provisions of the bill affecting the Franchise Tax Board (FTB).

PURPOSE OF THE BILL

According to the author's staff, the purpose of the bill is to increase the incentive for manufacturing businesses to remain or locate in California.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and would be operative for taxable years beginning on or after January 1, 2003.

POSITION

Pending.

ANALYSIS

<u>FEDERAL/STATE LAW</u>

Existing state and federal laws allow a taxpayer to deduct expenses paid or incurred in the ordinary course of a taxpayer's business and allow a depreciation deduction for the obsolescence or wear and tear of property used in a business or for investment property.

Existing federal law does not have a credit comparable to the MIC.

Existing state law allows qualified taxpayers a credit equal to 6% of the amount paid or incurred after January 1, 1994, for qualified property that is placed in service in California.

Board Position:			Department Director	Date
_______ S	_______ NA	_______ NP	Gerald H. Goldberg	01/31/03
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The MIC sunsets on January 1st of 2001 or the earliest subsequent year if the Employment Development Department determines that manufacturing (excluding aerospace) employment in California on the preceding January 1st does not exceed the January 1, 1994, employment level by at least 100,000 jobs. It is anticipated, based on current economic forecasts, that decreases in manufacturing employment may cause the MIC to sunset on January 1, 2004.

THIS BILL

This bill extends the repeal date of the MIC until at least January 1, 2006.

IMPLEMENTATION CONSIDERATIONS

Implementing this bill would not significantly impact the department's programs and operations.

TECHNICAL CONSIDERATIONS

This bill would delete subdivision (i) and renumber subdivisions (j) and (k) of Sections 17053.49 and 23649 of the Revenue and Taxation Code. Subdivisions (j) and (k) provide operative dates for changes made to the MIC since its original enactment. Since these subdivisions contain the phrase "the amendments made by the act adding this subdivision shall be operative" and this bill would renumber the subdivisions, taxpayers may have difficulty determining when the previous change became operative. The attached Amendments 1 through 4 would resolve this issue by citing the specific laws that changed the MIC.

Additionally, the legislatively mandated report entitled "Average Statewide Employment in Manufacturing (minus aerospace industries), Annual Report 2000," issued by the Employment Development Department, contains the observation that the change from using the Standard Industrial Classification (SIC) Code system to the North American Industry Classification System (NAICS) will make it impossible in 2003 to calculate a 2004 trigger that is consistent with the definitions and methods prescribed in the current Revenue and Taxation Code.

LEGISLATIVE HISTORY

SB 2X (Poochigian, 2003-2004) and SB 47 (Ackerman, 2003-2004) would remove the repeal date from the MIC, effectively extending the credit indefinitely. SB 2X is in the Senate Revenue and Taxation Committee awaiting a hearing date. SB 47 is in the Senate Rules Committee awaiting a hearing date.

AB 473 (Hertzberg, 1999-2000) would have extended the repeal date to January 1, 2004. AB 473 was held in the Senate Appropriations Committee.

AB 2145 (Knight; 1999-2000) would have removed the repeal date from the MIC, extending the credit indefinitely. SB 2145 was held in the Senate Revenue & Taxation Committee.

OTHER STATES' INFORMATION

The laws of the following states were reviewed because their tax laws are similar to California's income tax laws:

New York provides an investment tax credit (ITC) to manufacturers for certain depreciable equipment or buildings. The credit is 5% of up to $350 million of qualified expenditures and 4% for qualified expenditures in excess of $350 million. Certified pollution control, industrial waste treatment, and acid rain control facilities also qualify for this credit. Research and development (R&D) property may qualify for an optional rate of 9%.

Illinois provides a replacement tax investment credit equal to 0.5% of the basis of qualified property used by a taxpayer primarily engaged in manufacturing, retailing, coal mining, or fluorite mining.

Massachusetts provides a 3% credit based on the cost of qualified property used for manufacturing, farming, fishing, or research and development.

Michigan provides a graduated investment tax credit based on adjusted gross receipts of a firm. The credit is a percentage (0.85% to 2.3%) of the net costs of qualifying tangible, depreciable assets located in Michigan.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Revenue Estimate

The following revenue impact assumes that the Manufacturers' Investment Tax Credit (MIC) would become inoperative under current law starting with investments put in place 1/1/2004.

Estimated Revenue Impact For Investments Put In Place January 1, 2004 Through December 31, 2005 Assumed Enactment After June 30, 2003 (In Millions)		
2003-04	2004-05	2005-06
-$40	-$195	-$225

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this proposal.

Revenue Discussion

It is anticipated based on economic forecast that decreases in manufacturing employment are expected to cause the MIC to sunset on January 1, 2004. This bill would extend the repeal date until January 1, 2006, or January 1 of the earliest year thereafter, if total employment, as defined, in California does not exceed by 100,000 jobs the total employment in California on January 1, 1994. This estimate is based on a micro simulation model of California tax returns for taxable year 2000. These numbers were grown to approximate 2001 and beyond. The above estimate represents only that portion of applied credits with respect to newly generated credits pursuit to this bill. Prior year carryover credits will continue to be applied as allowed by prior law. Therefore, any revenue loss would be as a result of newly generated credits. The fiscal year cash flow patterns are based on the department's analysis of how manufacturers adjusted their tax payments to reflect the reduction in liability resulting from the current law MIC.

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO AB 122
As Introduced January 15, 2003

AMENDMENT 1

On page 19, modify line 17 as follows:

The amendments made by ~~the act adding this subdivision~~ Chapter 954 of the Statutes of 1996

AMENDMENT 2

On page 19, modify line 20 as follows:

The amendments made by ~~the act adding this subdivision~~ Chapter 323 of the Statutes of 1998

AMENDMENT 3

On page 30, modify line 35 as follows:

The amendments made by ~~the act adding this subdivision~~ Chapter 954 of the Statutes of 1996

AMENDMENT 4

On page 30, modify line 38 as follows:

The amendments made by ~~the act adding this subdivision~~ Chapter 323 of the Statutes of 1998